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The Effect of a Provision in an Insurance Policy Limiting the Authority of an Agent to Alter the Contract

IT has long been customary for insurance companies to insert in their policies restrictions on the authority of agents to change the insurance contract. It is the purpose of this article to consider the validity of such provisions.

The restrictive clause in the California Standard Form Fire Insurance Policy is: "and no officer, agent or other representative of this company shall have power to waive any provision or condition of this policy except by writing endorsed hereon or added hereto, and no person, unless duly authorized in writing, shall be deemed an agent of this company."¹

The number of different restrictive clauses that are now in use or have been used in the past is very great. The two commonest clauses in life insurance policies are: "No agent has power, in behalf of the company, to make or modify this or any contract of insurance, to extend the time for paying the premium, to waive any forfeiture, or to bind the company by making any promise, or by making or receiving any presentation or information":² and "Only the president, one of the vice-presidents, secretary, treasurer, auditor, or cashier has power on behalf of the

¹ This clause is very similar to that in the New York Standard Form Fire Insurance Policy, which reads: "and no officer, agent or other representative of this company shall have power to waive any provision or condition of this policy except such as by the terms of this policy may be the subject of agreement endorsed hereon or added hereto; and as to such provisions and conditions, no officer, agent or representative shall have such power, or be deemed or held to have waived such provisions or conditions, unless such waiver, if any, shall be written upon or attached hereto." The New York Standard Form Fire Insurance Policy is used in many states. Its use is mandatory in Arizona, Connecticut, Idaho, Louisiana, Nebraska, New Jersey, New York, North Dakota, Oklahoma, Oregon, Rhode Island, South Dakota, Texas, Washington, West Virginia and Wisconsin. See "Fire Insurance Laws, Taxes and Fees," published by The Spectator Company.

² In The Spectator Company's "Handy Guide to Premium Rates, etc.," for 1916 are given the policies of 167 life insurance companies. Of that number 37 contain no provision limiting the power of agents; 40,

company, and then only in writing, to make or modify this or any contract of insurance or to extend the time for paying any premium."³

Though the wording of the various restrictive clauses varies greatly, the particular phraseology used seems, except in a very few cases, to be unimportant. All the various clauses prohibit oral changes in the policy, and that is the only sort of change that brings the parties into court. So we may treat all the different clauses as if they were alike and merely provided: "No agent has authority to waive any provision of this policy except in writing."

What should be the effect of such a restriction on the power of an agent to waive orally a provision of the policy? At common law an agent has two kinds of authority, actual and ostensible. He has actual authority only to do those things which his principal expressly authorizes him to do. His implied or ostensible authority, however, is much greater. It permits him to do anything that is necessary or customary for the proper conduct of his agency. Expressing it in terms of the "reasonable third party fiction," an agent has ostensible authority to do anything which a reasonable third person, knowing the custom of the trade and the past practice of the agent, but not the principal's restrictions, would think that his principal had authorized him to do. This ostensible authority empowers an agent not only to do things as to which his principal has failed to instruct him, but also to go directly contrary to his principal's orders if only he acts as a reasonable third party, ignorant of the principal's instructions, would deem it reasonable for him to act.

Applying the common law rule to an agent with an insurance policy which prohibits him from changing it orally, what power has the agent so to change it? He has power to do whatever he

a provision worded in general like the first of the two given above; 80, a provision like the second of the two, but with many variations as to the particular officers named; while 20 contain both provisions.

³The following clauses have also been used extensively: "No officer, agent or other representative of the company shall have power to waive any provision or condition of the policy." "The use of general terms, or of anything less than a distinct, specific agreement, clearly expressed and endorsed upon this policy, shall not be construed as a waiver of any printed or written condition or restriction therein." "No alteration or waiver of any of the conditions of this policy shall be valid unless made in writing and signed by an officer of the company at the Home Office."

has actually been authorized to do. If the Insurance Company has in fact authorized him to modify the policy orally, it cannot hide behind a prohibition in the policy and repudiate such oral modifications as turn out not to be to its advantage. Such a provision, then, has no effect upon the actual authority of the agent, but should it not cut off completely his ostensible authority? It should. We can scarcely act on the assumption that it is not reasonable to expect a person who is buying insurance to read his policy, even if many people do not do so. And nobody can read the policy without realizing that the agent probably has not the authority he assumes to make oral changes in the printed contract.

The weight of authority, however, is to the effect that an agent, except a mere soliciting agent, has implied authority to orally change an insurance contract in the face of a provision in the policy to the contrary. The question has arisen in the Federal courts and in those of forty-four states. In some of the states decisions are conflicting and in others it is difficult to say what is the law, but probably the count stands: Against the validity of the limitation on the implied authority of the agent, 28 states;⁴

⁴None of the lists of cases are exhaustive except as to California. If the law of a state is well settled, usually only one case is given, while if the cases are in conflict or contain only dicta, several may be mentioned.

ALABAMA: *Continental Ins. Co. v. Brooks* (1901), 131 Ala. 614, 30 So. 876.

COLORADO: *German American Ins. Co. v. Hyman* (1908), 42 Colo. 156, 94 Pac. 27 (fire ins.); *Farmers and Merchants Ins. Co. v. Nixon* (1892), 3 Colo. App. 365, 30 Pac. 42.

CONNECTICUT: *Bernhard v. Rochester German Ins. Co.* (1906), 79 Conn. 388, 65 Atl. 134 (condition after loss); *Ward v. Metropolitan Life Ins. Co.* (1902), 66 Conn. 227, 33 Atl. 902.

ARKANSAS: *Queen of Arkansas Ins. Co. v. Forlines* (1910), 94 Ark. 227, 126 S. W. 719 (fire ins.); *Fidelity Mutual Life Ins. Co. v. Russell* (1905), 75 Ark. 25, 86 S. W. 814. Contra: *German American Ins. Co. v. Humphrey* (1896), 62 Ark. 348, 35 S. W. 428 (fire ins.); *Phoenix v. Public Parks Amusement Co.* (1896), 63 Ark. 187, 37 S. W. 959, (fire ins.). Contra, as to condition precedent to attachment of risk.

FLORIDA: *Southern States Fire Ins. Co. v. Vann* (1915), 69 Fla. 549, 68 So. 647.

ILLINOIS: *Phoenix Ins. Co. v. Grove* (1905), 215 Ill. 299, 74 N. E. 141, (fire ins.).

INDIANA: *West v. National Casualty Co.* (Ind. 1916), 112 N. E. 115 (dictum); *Hanover Fire Ins. Co. v. Dole* (1898), 20 Ind. App. 333, 50 N. E. 772.

INDIAN TERRITORY: *German American Ins. Co. v. Paul* (1904), 5 Ind. T. 703, 83 S. W. 60, (dictum).

IOWA: *Liquid Carbonic Acid Mfg. Co. v. Phoenix Ins. Co.* (1904), 126 Iowa 225, 101 N. W. 749. (fire ins.) Contra: *Mulrooney v. Royal*

in favor of its validity, 16 states⁶ and the Federal courts. With the

Ins. Co. (1908), 163 Fed. 833, (fire ins.).

KANSAS: Phoenix Ins. Co. v. Munger (1892), 49 Kan. 728, 30 Pac. 120; German Ins. Co. v. Gray (1890), 43 Kan. 497, 23 Pac. 637, (fire ins.).

KENTUCKY: New England Mutual Life Ins. Co. v. Springgate (1908), 129 Ky. 627, 112 S. W. 681; German American Ins. Co. v. Yellow Poplar Lbr. Co. (Ky. 1905), 84 S. W. 551 (fire ins.).

MAINE: Bigelow v. Granite State Fire Ins. Co. (1900), 94 Me. 39, 46 Atl. 808.

MICHIGAN: Kotwicki v. Thuringa Ins. Co., (1903), 134 Mich. 82, 95 N. W. 976, (fire ins.); Beebe v. Ohio Farmers Ins. Co. (1892), 93 Mich. 514, 53 N. W. 818 (fire ins.). Contra: Cleever v. Traders Ins. Co., (1887), 65 Mich. 527, 32 N. W. 660, (fire ins.).

MINNESOTA: Leland v. Modern Samaritans (1910), 111 Minn. 207, 126 N. W. 728 (life ins.); Andrus v. Maryland Casualty Co. (1904), 91 Minn. 358, 98 N. W. 200, (indemnity ins.); Lamberton v. Continental Fire Ins. Co. (1888), 39 Minn. 129, 39 N. W. 76.

MISSISSIPPI: London Guarantee & Accident Co. v. Mississippi Central Ry. Co. (1910), 97 Miss. 165, 52 So. 787, (employers' liability ins.); Liverpool & London & Globe Ins. Co. v. Sheffy (1894), 71 Miss. 919, 16 So. 307, (fire ins.).

MISSOURI: James v. Mutual Reserve Fund Life Ass'n. (1898), 148 Mo. 1, 49 S. W. 978.

NEBRASKA: Hunt v. State Ins. Co. (1902), 66 Neb. 121, 92 N. W. 921, (fire ins.); Hartford Fire Ins. Co. v. Landfare (1902), 63 Neb. 559, 88 N. W. 779. Contra: Burlington Ins. Co. v. Campbell (1894), 42 Neb. 208, 60 N. W. 599.

NEW HAMPSHIRE: Spalding v. New Hampshire Fire Ins. Co. (1902), 71 N. H. 441, 52 Atl. 858; Perry v. Dwelling House Ins. Co. (1892), 67 N. H. 291, 33 Atl. 731.

NORTH CAROLINA: Gwaltney v. Provident Savings Life Ins. Soc. (1903), 132 N. C. 925, 44 S. E. 659.

OKLAHOMA: Springfield Fire & Marine Ins. Co. v. Halsey (Okl. 1915), 153 Pac. 145; Germania Fire Ins. Co. v. Barringer (1914), 43 Okl. 279, 142 Pac. 1026; Modern Woodmen of America v. Weekley (1914), 42 Okl. 25, 139 Pac. 1138, (life ins.). Contra: Phoenix Ins. Co. v. Ceaphus (1911), 29 Okl. 608, 119 Pac. 583, (fire ins.).

SOUTH CAROLINA: L. T. Madden & Co. v. Phoenix Assur. Co. (1904), 70 S. C. 295, 49 S. E. 855, (fire ins.); Wilson v. Commercial Union Assur. Co. (1898), 51 S. C. 506, 29 S. E. 245, (fire ins.).

SOUTH DAKOTA: Fosmark v. Equitable Fire Ass'n (1909), 23 S. D. 102, 120 N. W. 777; Vesey v. Commercial Union Assur. Co. (1904), 18 S. D. 632, 101 N. W. 1074, (fire ins.).

TENNESSEE: Aetna Life Ins. Co. v. Fallon (1903), 110 Tenn. 720, 77 S. W. 937.

TEXAS: First Texas State Ins. Co. v. Capers (Tex. 1916), 183 S. W. 794 (life ins.); Aetna Ins. Co. v. Eastman (Tex. Civ. App. 1094), 80 S. W. 255, (fire ins.).

UTAH: West v. Norwich Union Fire Ins. Soc. (1894), 10 Utah 442, 37 Pac. 685.

VIRGINIA: Virginia Fire & Marine Ins. Co. v. Richmond Mica Co. (1904), 102 Va. 429, 46 S. E. 463.

VERMONT: Wilson v. Commercial Union Assur. Co. (1916), 90 Vt. 105, 96 Atl. 540, (fire ins.); Frost v. North British Mer. Ins. Co. (1905), 77 Vt. 407, 60 Atl. 803, (dictum).

WYOMING: Kahn v. Traders Ins. Co. (1893), 4 Wyo. 419, 34 Pac. 1059, (fire ins.).

⁶ CALIFORNIA: Elliott v. Frankfort Marine etc. Ins. Co. (1916), 172

minority are several of the most influential courts, among others those of California, Massachusetts, New York, Ohio and Pennsylvania, and the Supreme Court of the United States.

Cal. 261, 156 Pac. 481; *Westphall v. Metropolitan Life Ins. Co.* (1915), 27 Cal. App. 734, 151 Pac. 155; *Madsen v. Maryland Casualty Co.* (1914), 168 Cal. 204, 142 Pac. 51; *Belden v. Union Central Life Ins. Co.* (1914), 167 Cal. 740, 141 Pac. 370; *Sharman v. Continental Ins. Co.* (1914), 167 Cal. 117, 138 Pac. 708; *Raulet v. Northwestern etc. Ins. Co.* (1910), 157 Cal. 213, 107 Pac. 292; *Bank of Anderson v. Home Ins. Co.* (1910), 14 Cal. App. 208, 111 Pac. 507; *McCullough v. Home Ins. Co.* (1909), 155 Cal. 659, 102 Pac. 814; *Iverson v. Metropolitan Life Ins. Co.* (1907), 151 Cal. 746, 91 Pac. 609; *Mackintosh v. Agricultural Fire Ins. Co.* (1907), 150 Cal. 440, 89 Pac. 102; *Cayford v. Metropolitan Life Ins. Co.* (1907), 5 Cal. App. 715, 91 Pac. 266; *Arnold v. American Ins. Co.* (1906), 148 Cal. 660, 84 Pac. 182; *Knarston v. Manhattan Life Ins. Co.* (1903), 140 Cal. 57, 73 Pac. 740; *Westerfeld v. New York Life Ins. Co.* (1900), 129 Cal. 68, 61 Pac. 667; *West Coast Life Co. v. State etc. Co.* (1893), 98 Cal. 502, 33 Pac. 258; *Farnum v. Phoenix Ins. Co.* (1890), 83 Cal. 246, 23 Pac. 869; *Wheaton v. Ins. Co.* (1888), 76 Cal. 415, 18 Pac. 758; *Carroll v. Girard Fire Ins. Co.* (1887), 72 Cal. 297, 13 Pac. 863; *Enos v. Sun Insurance Co.* (1885), 67 Cal. 621, 8 Pac. 379; *Silverberg v. Phoenix Ins. Co.* (1885), 67 Cal. 36, 7 Pac. 38; *Gladding v. Cal. Farmers' Mutual Fire Insurance Co.* (1884), 66 Cal. 6, 4 Pac. 764; *Shuggart v. Lycoming Fire Ins. Co.* (1880), 55 Cal. 408. *Contra: Mackintosh v. Agricultural Fire Ins. Co.* (1907), 150 Cal. 440, 89 Pac. 102.

DELAWARE: *Cohen v. Home Insurance Co.* (Del. 1916), 97 Atl. 1014 (fire ins.). *Contra* as to condition precedent to attachment of risk.

GEORGIA: *Nowell v. British American Assur. Co.* (1915), 17 Ga. App. 46, 85 S. E. 498 (fire ins.); *Lippman v. Aetna Ins. Co.* (1899), 108 Ga. 391, 33 S. E. 897 (fire ins.)

LOUISIANA: *Murphy v. Royal Ins. Co.* (1899) 52 La. Ann. 775, 27 So. 143 (fire ins.)

MARYLAND: Dicta in the following cases: *Bakhaus v. Caledonian Ins. Co.* (1910), 112 Md. 676, 77 Atl. 310; *Dulany v. Fidelity & Casualty Co.* (1907), 106 Md. 17, 66 Atl. 614; *Farmers Fire Ins. Co. v. Baker* (1902), 94 Md. 545, 51 Atl. 184; *Hartford Fire Ins. Co. v. Keating* (1897), 86 Md. 130, 38 Atl. 29.

MASSACHUSETTS: *Harris v. North America Ins. Co.* (1906), 190 Mass. 361, 77 N. E. 493, (fire ins.).

MONTANA: *Collins v. Metropolitan Life Ins. Co.* (1905), 32 Mont. 329, 80 Pac. 609.

NEW JERSEY: *Wheeler v. U. S. Casualty Co.* (1904), 71 N. J. Law 396, 59 Atl. 347, (accident ins.); *Snyder v. Dwelling House Ins. Co.* (1897), 59 N. J. Law 18, 37 Atl. 1022. *Contra* as to conditions after loss.

NEW YORK: *Tilton v. Farmers Ins. Co.* (1913), 143 N. Y. Supp. 107 (fire ins.); *Baumgartel v. Providence Washington Ins. Co.* (1893), 136 N. Y. 547, 32 N. E. 990, (fire ins.).

OHIO: *Ohio Farmers Ins. Co. v. Titus* (1910), 82 Ohio St. 161, 92 N. E. 82, (fire ins.).

OREGON: *Egan v. Westchester Fire Ins. Co.* (1895), 28 Ore. 289, 42 Pac. 611.

PENNSYLVANIA: *Lantz v. Vermont Life Ins. Co.* (1891), 139 Pa. St. 546, 21 Atl. 80. *Contra* as to conditions precedent to the attaching of the risk. *McDonigle v. Susquehanna Mutual Fire Ins. Co.* (1895), 168 Pa. St. 1, 31 Atl. 868; *Dwelling House Ins. Co. v. Gould* (1890), 134 Pa. St. 570, 19 Atl. 793.

RHODE ISLAND: *Reed v. Equitable Fire & Marine Ins. Co.* (1892), 17 R. I. 785, 24 Atl. 833.

The minority courts defend their decisions by applying the common law of agency to the insurance contract. They would all approve of the statement of the Superior Court of Delaware in *Cohen v. Home Insurance Company*.⁶

"No rule is better settled than where a limitation on the power of an agent is brought home to the person dealing with him, such person relies upon any act in excess of such limited authority at his peril, and hence when an insurance company limits the power of its agent and notice of such limitation is brought home to the person dealing with him, it is not bound by any act of the agent in contravention of the notice."

The reasoning of the courts that refuse to apply the common law of agency to a provision in an insurance policy limiting the authority of an agent to alter the contract takes many forms. One of the commonest arguments is that of the Supreme Court of Kentucky in *German American Insurance Company v. Yellow Poplar Library Company*.⁷ "A contract of insurance is not within the statute of frauds. It is not necessary that it should be in writing, and although in writing it may be changed by parol

UNITED STATES SUPREME COURT: *Lumber Underwriters v. Rifle* (1915), 237 U. S. 605, 59 L. Ed. 1140, 35 Sup. Ct. Rep. 717 (fire ins.); *Penman v. St. Paul Fire & Marine Ins. Co.* (1910), 216 U. S. 311, 54 L. Ed. 493, 30 Sup. Ct. Rep. 312, (fire ins.); *Northern Assur. Co. v. Grand View Building Ass'n* (1902), 183 U. S. 308, 46 L. Ed. 213, 22 Sup. Ct. Rep. 133, (fire ins.); *Slocum v. New York Life Ins. Co.* (1913), 228 U. S. 364, 57 L. Ed. 900, 33 Sup. Ct. Rep. 523.

WASHINGTON: *Nixon v. Travelers Ins. Co.* (1901), 25 Wash. 254, 65 Pac. 195, (life ins.). Contra: *Henschel v. Oregon Fire & Marine Ins. Co.* (1892), 4 Wash. 476, 30 Pac. 735.

WEST VIRGINIA: *Ritchie County Bank v. Fireman's Ins. Co.* (1904), 55 W. Va. 261, 47 S. E. 94. Contra: *Woolfert v. Franklin Ins. Co.* (1896), 42 W. Va. 647, 26 S. E. 521, (fire ins.); *Koles v. Jefferson Ins. Co.* (1895), 41 W. Va. 261, 23 S. E. 732, (fire ins.).

WISCONSIN: *Woodard v. German American Ins. Co.* (1906), 128 Wis. 1, 106 N. W. 681, (fire ins.); *Welch v. Fire Ass'n of Philadelphia* (1904), 120 Wis. 456, 98 N. W. 227, (fire ins.).

⁶ (Del. 1916), 97 Atl. 1014. Similar reasoning is found in *Ohio Farmers Ins. Co. v. Titus* (1910), 82 Ohio St. 161, 92 N. E. 82; *Murphy v. Royal Ins. Co.* (1910), 52 La. 775, 27 So. 143; *Lantz v. Vermont Ins. Co.*, (1891), 139 Pa. 546, 21 Atl. 80; *Slocum v. New York Life Ins. Co.* (1913), 228 U. S. 364, 57 L. Ed. 900, 33 Sup. Ct. Rep. 523.

⁷ 84 S. W. 551. Similar reasoning is found in *Aetna Accident & Liability Co. v. White* (Texas 1915), 177 S. W. 162; *West v. Norwich Fire Ins. Soc.*, (1894), 10 Utah 442, 37 Pac. 685; *Aetna Life Ins. Co. v. Fallon* (1903), 110 Tenn. 720, 77 S. W. 937; *Phoenix Ins. Co. v. Munger* (1892), 49 Kan. 178, 30 Pac. 120; *German Ins. Co. v. Gray* (1890), 43 Kan. 497, 23 Pac. 637; *Gwaltney v. Provident Savings Life Assurance Co.*, (1903), 132 N. C. 925, 44 S. E. 659.

even though the contract provides that it shall only be changed by writing."

All perfectly true. But what of it? Of course it would be carrying freedom of contract to an absurdity to allow me to bind myself never to make a contract except in writing. But from this it does not follow that, providing I notify you, I cannot limit the power of my agent to alter orally the contract that you and I have made. That I may do this in a building contract is well settled. It has been customary for years to provide in large building contracts that the owner need pay for no extras or alterations unless they are ordered by the architect in writing. If the owner orally orders the alterations he must pay for them, but if his architect does so, he need not, because he may limit the power of his agent to contract orally, but not his own.⁸

One of the most interesting cases on the subject of parol waivers is *Hunt v. State Insurance Company*.⁹ In this case the court had decided that a provision in a policy of insurance that no officer or agent shall be held to have waived any of its terms or conditions unless such waiver shall be endorsed thereon in writing is a limitation on the authority of a local agent of the company, and an attempted waiver in violation of such a provision is not binding on the company. A rehearing was granted. The opinion on rehearing was written by Dean Pound of the Harvard Law School, who since the first hearing of the case had been appointed Supreme Court Commissioner of Nebraska. Commissioner Pound reasoned as follows: The policy provided that it should be forfeited if the premises became unoccupied. This meant that the company had the option of forfeiting the policy if this contingency occurred. The premises became unoccupied. An agent of the company was notified. Notice to the agent was notice to the company. Thereafter the company endorsed a mortgage clause on the policy. By endorsing the mortgage clause on the policy after notice of a ground of forfeiture, the company waived the forfeiture. A waiver by the company itself need not be in

⁸ See building contract cases *infra*.

⁹ (1902), 66 Neb. 121, 92 N. W. 921. Similar reasoning is found in *Hartford Fire Ins. Co. v. Landfare* (1902), 63 Neb. 559, 88 N. W. 779; *Kahn v. Traders Ins. Co.* (1893), 4 Wyo. 419, 34 Pac. 1059; *Niagara Ins. Co. v. Lee*, (1889), 73 Tex. 641, 11 S. W. 1024; *Southern States Fire Ins. Co. v. Vann* (1915), 69 Fla. 549, 68 So. 647.

writing, and so the provision in the policy against waivers is avoided.

If Dean Pound's reasoning is correct, our problem is solved unless the insurance companies are inconsiderate enough to change the wording of their policies to prevent the knowledge of the agent being the knowledge of the principal. This some companies have already done.¹⁰

In conditional sale contracts of farming machinery, a provision that notice of any defect or of election to rescind must be sent to the Home Office as well as to the agent is commonly inserted in the contract and has usually been held to prevent notice to the agent being notice to the company.¹¹

Dean Pound's reasoning reaches a result that is contrary to the intent of the parties, or rather, of the insurance company, for in the vast majority of cases the insured has no intent on the subject and the printed policy would not be changed to comply with his wishes if he had any. This reasoning has been adopted by only a very few of the courts dealing with this problem. It has never been alluded to in the building contract cases. In these cases it is provided that the owner need pay for no extras unless they are ordered by the architect in writing. The owner can waive the requirement of a written order just as easily as the insurance company can the forfeiture of a policy. If the knowledge of the architect is the knowledge of the owner, the owner knows that his agent, the architect, has ordered the extras, and that the contractor is furnishing them relying upon his oral order. If with this knowledge the owner receives the extras, that is, allows them to be attached to his building and thereby become a part of his realty, he ought to be held, on Dean Pound's reasoning, to have waived the requirement of a writing, but the courts do not so hold.

The place where the reasoning of the Hunt case would work the greatest change in the law is not in insurance or building contract cases, for there it would undoubtedly be met by a change in the wording of the clause in the contract further restricting the power of the agent, but in the ordinary common law case.

I give my agent authority to sell my horse for not less than

¹⁰ *Andrus v. Maryland Casualty Co.*, (1904), 91 Minn. 358, 98 N. W. 200. The provision in this case was held invalid.

¹¹ See conditional sale contracts *supra*.

one hundred dollars. The purchaser knows of this limitation on my agent's authority, but buys the horse for eighty dollars, which he hands to the agent. I am unable to see why, on the reasoning of the Hunt case, there has not been a valid sale. The knowledge of the agent is that of the principal. The sale is one which the principal could ratify if he so desired, for even if a stranger sells my horse I can ratify the sale if I so choose. The principal has received the purchaser's money, because receipt by the agent is receipt by the principal, or perhaps the agent has actually turned over the money to his principal, the latter supposing his agent had received it as the purchase price of another horse that he had authority to sell for eighty dollars. If the knowledge of the agent is the knowledge of the principal in such a case, the ability of the principal to protect himself from the improper acts of his agent by notifying third parties of the limitations on the agent's authority is greatly curtailed.

I know of no case stating that the knowledge of the agent is not that of the principal if the third party knows that the agent is exceeding his authority, but there are plenty of cases holding that no title passes in situations like the horse case just referred to.¹² It is well established that if the third party knows that the agent is committing a fraud on his principal, the knowledge of the agent is not that of the principal.¹³

In cases like the Hunt case the insured notifies the agent that the premises will be unoccupied. The insured would know, if he read his policy and could understand it, that upon the receipt of that information it was the duty of the agent to put the proper indorsement on the policy or else to cancel it. Further, when the insured paid the next premium, and some agent received it without making the proper indorsement on the policy, he would know either that the agent was acting improperly, or else did not know of the ground of forfeiture. But is it not desirable that thousands of people take out insurance who have not intellectual acumen enough to understand the terms of their policies, much less to realize that when they are satisfied with the oral permission of an agent they are permitting the agent to disregard the orders of his principal? This is the real question at

¹² 2 C. J. 598; *Mechem on Agency*, §§ 854, 922.

¹³ 2 C. J. 871, and cases there cited; 2 *Mechem on Agency*, § 1826.

issue between the majority and the minority: Which rule is the better in the light of public policy?

The argument against the public policy of allowing the insurance company to limit the authority of its agent is ably stated by Judge Dunbar in his concurring opinion in *Nixon v. Travelers' Insurance Company*.¹⁴

"I concur in the result, for the reason that the record shows that the assured had actual knowledge, outside of the stipulation in the policy, of the limitations on the agent's authority, but not on the ground stated in the majority opinion. I make no question of the correctness of the rule stated in relation to the general law of agency, but do not think the strict rule ought to apply to insurance and other similar companies which do their business exclusively through agents. In such cases all the actors are necessarily agents. The company is composed of agents; and persons who contract with the company will, in spite of all theories of law, rely upon the statements of such agents, and will regard them as the company. They will not scrutinize closely all the conditions contained in the body of the policy, and could not understand many of them if they did. They will rely upon the statements of the agents appointed by the company, and who come to deal with them armed with the recommendations of the company; and innocent parties, who act on their advice, ought not to suffer. In addition to this the contracts are in a sense one-sided. They are prepared in advance by the agents of the company, without any consultations with or consideration by the assured, and they place the parties in a different position, so far as responsibility is concerned, from the ordinary mutual contract or agreement made and entered into between individuals."

Judge Dunbar might well have added that the company will not change the wording of its policy to please the would-be insured, and the only choice open to him is to take the policy offered to him or to go without protection.¹⁵

If Judge Dunbar's view of public policy is correct, the fact that the insured has actual knowledge of the limitation on the authority of the agent should not bar his recovery.

The New York standard fire insurance policy¹⁶ has the

¹⁴ 25 Wash 294, (1901), 65 Pac. 195. Similar reasoning is found in *Wilson v. Commercial Union Assur. Co.* (Vt. 1916), 96 Atl. 540; *Farmers & Merchants Ins. Co. v. Nixon* (1892), 2 Colo. App. 365, 30 Pac. 42.

¹⁵ *Wilson v. Commercial Union Assur. Co.* supra, n. 14.

¹⁶ Prescribed by law in 16 states.

clause limiting the agent's authority at the end of the policy in heavy type. The California standard fire insurance policy has the clause at the bottom of the first page just above the signature of the company's representative. Nearly all the life insurance policies either have the clause in a very prominent position or else preceded by some such heading as "Powers of Agents" in large letters. So that usually, if the insured even glances through his policy, he cannot help noting the limitation on the agent's authority.

Public policy certainly does not necessitate the insured's swearing that he signed the paper without knowing whether it was an insurance policy or a gift deed of all he owned, as a prerequisite to recovery. The real basis of recovery, as stated by Judge Dunbar, is that the insured is forced to accept a policy containing many terms far beyond his comprehension, and that the agent of the company is the natural and proper person for him to turn to for their interpretation.

In favor of the common law rule allowing the limitation on the agent's authority are also weighty considerations of public policy. The insurance companies are no more able to prevent misrepresentations of their agents than the railways are the negligence of theirs. The companies will take into account the loss they suffer through the improper conduct of their agents in determining their rates. Thus the result of making the companies liable for the oral misrepresentations of their agents will be to make those of the insured who have the ability and take the time to decipher their policies pay for the negligence or inability of the others. Further, very often the effect of the reliance of the insured upon an oral representation or permission given him by the agent is to give him insurance below the established tariff; in terms of railway rates, to give him a rebate. Insurance rebates are, of course, against public policy, but not so strongly as are railway rebates, for while the latter are procured by the strongest competitors and enable them to drive out the others, the former are almost invariably obtained by the weaker members of society.

The reason any insurance agent would give you for inserting in the policy limitations on his authority is that the company suspects of being dishonest not him but the insured. Cheating life insurance companies, for example, would be poor sport if you had to have a written statement from the company before

claiming that, although you paid the premium appropriate to an Olympic champion, nevertheless the company knew that you were dying of consumption and that your representations to the contrary were made merely because the agent told you it didn't matter what you answered. If the companies are not allowed to require all the terms of the insurance contract to be in writing, it is almost impossible for them to prevent a large amount of fraud. It is well recognized among attorneys for insurance companies that, no matter what evidence they produce, the jury will always believe the insured. Insurance agents are not selected from ex-convicts, and it is beyond belief that it is always they who do the lying. Of course the difficulty of preventing the insured from defrauding them if they cannot limit their agent's authority is not a sufficient reason for allowing the companies to limit the authority of their agents and thereby defraud the insured. Furthermore, the general policy of the law today is to give greater rather than less effect to oral acts and representations as distinguished from those made more formally. Nevertheless, the danger of their being defrauded by manufactured parol testimony which the jury will almost certainly believe should be considered before deciding that public policy requires that insurance companies be deprived of an effective means of preventing fraud which the common law allowed them and which the law still allows persons in all other lines of activity.

This argument would, however, have been entitled to more weight ten years ago than today. The chance of an insurance company, especially a life insurance company, receiving fair treatment in court is much greater today than then. The insurance companies are placing greater value on the good will of the public and changing their methods of business accordingly. "We are not insisting on technicalities to the extent we once did," said one life insurance agent. The judges and juries are commencing to realize this change and to give the companies, especially the life insurance companies, better treatment.

Nevertheless, the fact that the law still allows persons engaged in any business but insurance to limit the power of their agents to change their contracts is, if true, a very strong argument in favor of the common law rule. I have been able to find but two other classes of contracts in which such limitations are com-

monly inserted, viz., building contracts and conditional sales or sales on approval contracts.

When constructing a large building the owner usually employs an architect to draw up plans, hire contractors, supervise their work and act as arbitrator in all disputes between them and the owner. The architect is usually given power to order extra work or omissions within very wide limits. The one curb regularly put upon his authority is that no work not required by the plans and specifications shall be paid for unless ordered by the architect in writing.

If there is a provision in the contract requiring a written order from the architect, can the contractor recover for extras done without one? I have been able to find only fifteen states in which this question has been decided by appellate courts. In all but three of them the contractor would probably be denied recovery.¹⁷ The weight of authority is thus directly contrary to the way it is in insurance cases. In general, if the courts of a state hold that a provision limiting the authority of agents to change the contract orally is valid in an insurance contract, they hold a similar provision in a building contract valid, and vice versa. Texas, however, holds such a provision invalid in an insurance contract and valid in a building contract, while if it is fair to judge the law of a state from a single decision of the federal court, Virginia and West Virginia hold just the opposite, that the provision is valid in an insurance contract, but not in a

¹⁷ CALIFORNIA: *Brookings Lumber & Box Co. v. Manufacturers Automatic Sprinkler Co.* (1916), 173 Cal. 679, 161 Pac. 266. *Gray v. La Societe Francaise Etc.* (1901), 131 Cal. 566, 63 Pac. 848. *J. M. Griffith Company v. City of Los Angeles* (1898), 6 Cal. Unrep. 119, 54 Pac. 383. *White v. San Rafael & San Quentin R. R. Co.* (1875), 50 Cal. 417; *McFadden v. O'Donnell* (1861), 18 Cal. 160.

GEORGIA: *Heard v. Dooly Co.* (1897), 101 Ga. 619, 28 S. E. 986.

ILLINOIS: *Stubbins v. World's Columbian Exposition Co.* (1903), 110 Ill. App. 210. *Joslyn v. City of Elgin* (1887), 36 Ill. App. 301. Affirmed (1891), 136 Ill. 525, 26 N. E. 1090.

INDIANA: *Duncan v. Board of Commissioners* (1862), 19 Ind. 154.

LOUISIANA: *Winston Bros. & Co. v. Louisinna Cent. Const. Co.* (1910), 127 La. 10, 53 So. 367. *Monarch v. Board of Commissioners* (1897), 49 La. App. 991, 22 So. 259.

MARYLAND: *McNulty v. Keyser Office Bldg. Co.*, (1910), 112 Md. 638, 76 Atl. 1113 (1 & 2).

MASSACHUSETTS: *Millen v. City of Boston* (1914), 218 Mass. 181, 105 N. E. 453. *Stuart v. City of Cambridge* (1878), 125 Mass. 102.

MONTANA: *Piper v. Murray* (1911), 43 Mont. 230, 115 Pac. 669.

NEBRASKA: *McGowan v. Gate City Malt Co.* (1911), 89 Neb. 10, 130 N. W. 965. *Campbell v. Kimball* (1910), 87 Neb. 309, 127 N. W. 142. *Carter v. Root* (1909), 84 Neb. 723, 121 N. W. 952.

building contract. Thus it is possible that the reason the weight of authority is on opposite sides of our question in insurance and building contract cases is that building contract cases have not arisen in states that hold limitations on the authority of agents invalid in insurance contracts.

The opportunity for one party to overreach the other is perhaps not so great in big building contracts as in insurance contracts, but it is still very great. The ability of the owner to force the contractor to accept a contract providing that the owner's agent, the architect, shall be the sole arbitrator of all disputes, shows the inequality of the parties in bargaining power. The fact that the contractor understands the meaning of the contract and realizes that he will be at the mercy of a dishonest owner and architect, but signs the contract because competition makes it impossible for him to get a better one, is no reason why the courts should not be as willing to protect him as an insured who does not realize what he is getting into.

In conditional sale or sale on approval contracts, the situation of the parties is very similar to that in insurance contracts. The great majority of such cases in which the question has arisen have been cases of sales of farming machinery. In them you have on the one side a powerful corporation, like the International Harvester Company, that is selling its machines on contracts which are drawn up with great care at the home office, through agents whose earnings depend upon the number of sales they make and who thus have just as much reason as an insurance agent to try to overstep the purchaser. On the other side of the contract you have a farmer who presumably has had little education and will not hire a lawyer. He must be in modest circumstances or he would secure the cash discount obtainable by purchasing his farming machinery outright. He probably is very much in need of a machine to help him harvest his crops and has had little if any experience with harvesting machinery and is utterly unable to tell in advance a good machine from a bad one. When such a person comes into court and says the agent told him that the machine would thresh forty bushels of wheat a day and he could not tell from the long contract in very small print just what the machine was warranted to do, I should think the courts would be just as willing to grant him relief as if he were an insured alleging that he had been misled by the agent of a

powerful insurance company. In twenty-one states I have found cases dealing with the power of an agent under a conditional sale contract providing that no agent shall have authority to modify the contract except in writing. In sixteen states such a provision is held valid,¹⁸ while five states are contra.¹⁹ In ten of the sixteen states, a similar provision in an insurance contract is held invalid.

NEW JERSEY: *Landstra v. Bunn* (1911), 81 N. J. Law 690, 80 Atl. 496; *Sheyer v. Pinkerton Cons. Co.* (1904), 59 Atl. 462.

NEW YORK: *Traitel Marble Co. v. Brown Bros.* (1913), 144 N. Y. Supp. 562; *Kelly v. St. Michael's Roman Catholic Church* (1912), 133 N. Y. Supp. 328; *Langley v. Rouse* (1906), 185 N. Y. 201, 77 N. E. 1168. OHIO: *Baltimore & Ohio R. Co. v. Jolly Bros. & Co.* (1904), 71 Ohio 92, 72 N. E. 888.

PENNSYLVANIA: *Gibbs v. School Dis.* (1900), 195 Pa. 476, 46 Atl. 91.

TEXAS: *Taub v. Woodruff* (Tex. 1910), 134 S. W. 750; *Ferrier v. Knox County* (Tex. 1896), 33 S. W. 896.

WASHINGTON: *Wiley v. Hart* (1913), 174 Wash. 142, 132 Pac. 1015.

WISCONSIN: *McGrath Const. Co. v. Waupaca-Green Bay Ry. Co.* (1912), 148 Wis. 372, 134 N. W. 824.

FEDERAL: *Caldwell & Drake v. Schmulbach* (1909), 175 Fed. 429; *Jefferson Hotel Co. v. Brumbaugh* (1909), 168 Fed. 867.

¹⁸ ALABAMA: *Fulton v. Sword Medicine Co.* (1906), 145 Ala. 331, 40 So. 393. *Capital Security Co. v. Owen* (Ala. 1916), 72 So. 8.

GEORGIA: *McCormick Harv. Mach. Co. v. Allison* (1902), 116 Ga. 442, 42 S. E. 778.

ILLINOIS: *Eichelroth v. Long* (1908), 156 Ill. App. 108; *Irle v. Nichols & Shepard Co.* (1900), 89 Ill. App. 619.

INDIANA: *Bragg v. Bamberger* (1864), 23 Ind. 198.

KENTUCKY: *Second National Bank of Richmond v. Adams* (1906), 93 S. W. 671.

LOUISIANA: *Advance Thresher Co. v. Roger* (1909), 123 La. 1067, 49 So. 709.

MASSACHUSETTS: *Colonial Development Corporation v. Bragdon* (1914), 219 Mass. 170, 106 N. E. 633.

MINNESOTA: *Larson v. Minneapolis Threshing Machine Co.* (1904), 92 Minn. 62, 99 N. W. 623.

MISSOURI: *Gaar, Scott & Co. v. Nelson* (1912), 166 Mo. App. 51, 148 S. W. 417; *Nichols-Shepard Co. v. Rhoadman* (1905), 112 Mo. App. 299, 87 S. W. 62.

NEW YORK: *Metropolitan Aluminum Mfg. Co. v. Lau* (1908), 112 N. Y. Supp. 1059; *Flower City Plant Food Co. v. Roberts* (1903), 80 N. Y. Supp. 1060.

NORTH CAROLINA: *J. I. Case Threshing Mach. Co. v. McClamrock et al.* (1910), 152 N. C. 405, 67 S. E. 991; *Thompson v. Green River Power Co.* (1910), 154 N. C. 13, 69 S. E. 756.

NORTH DAKOTA: *Westby v. J. I. Case Threshing Mach. Co.* (1911), 21 N. D. 475, 132 N. W. 137; *Coleau Mfg. Co. v. Blanchett* (1910), 16 N. D. 341, 113 N. W. 614; *Case Threshing Machine Co. v. Erbighausen* (1902), 11 N. D. 466, 92 N. W. 826.

SOUTH DAKOTA: *Reeves & Co. v. Lewis et al.* (1910), 25 S. D. 44, 125 N. W. 289.

TEXAS: *Fetzer v. Haralson* (1912), 147 S. W. 290; *J. I. Case Threshing Machine Co. v. Hall* (1903), 73 S. W. 835; *Blackstad Merchantile Co. v. J. W. Porter & Co.* (1913), 158 S. W. 216.

UTAH: *Consolidated Wagon & Machine Co. v. Barben* (1915), 46 Utah 377, 150 Pac. 949.

So far we have assumed that there was already an existing contract between the parties, but the same problem may arise before the contract has been entered into. For example, the policy may make it a condition precedent to the attachment of the risk that the insured be the owner in fee of the premises in question. The property is mortgaged, but the insured claims the agent told him at the time he took out the policy that fact was immaterial. Can the insured show this oral modification in the printed form of contract in the face of a provision that no agent has authority to vary any provision of this policy except in writing? Here we have all the questions which we have been considering, and, in addition, the problem of the parol evidence rule, for the insured is offering prior or contemporaneous negotiations for the purpose of varying, contradicting or adding to the written contract. The Supreme Court of the United States will not let the insured do this. It has said, through Mr. Justice Holmes in *Lumber Underwriters v. Rife*:²⁰

"Therefore, when, by its written stipulation the document gave notice that a certain term was insisted upon, it would be contrary to the fundamental theory of the legal relations established to allow parol proof that at the very moment when the policy was delivered that term was waived. . . . No rational theory of contract can be made that does not hold the assured to know the contents of the instrument to which he seeks to hold the other party."

But the weight of authority is against the Supreme Court.²¹ The majority of the courts are not only willing to change the common law of agency for the benefit of the insured, but also to do away with the parol evidence rule, a rule itself founded on public policy and established for the purpose of preventing fraud. This violation of the parol evidence rule can only be justified

WEST VIRGINIA: *Fruit Dispatch Co. v. Ellis* (1914), 75 W. Va. 52, 83 S. E. 187.

¹⁹ IOWA: *First National Bank v. Dutcher* (1905), 128 Iowa 413; 104 N. W. 497; *Reeves & Co. v. Younglove* (1910), 148 Iowa 699 127 N. W. 1017.

KANSAS: *Nichols & Shepard Co. v. Maxon* (1907), 76 Kan. 607, 92 Pac. 545.

MICHIGAN: *Challenge Wind & Feed Mill Co. v. Kerr* (1892), 93 Mich. 328, 53 N. W. 555.

NEBRASKA: *McCormick Harvesting Mach. Co. v. Hiatt* (1903), 4 Neb. (unof.) 587, 95 N. W. 627.

WISCONSIN: *Bannon v. C. Aultman & Co.* (1891), 80 Wis. 307, 49 N. W. 967.

²⁰ (1915), 237 U. S. 605, 59 L. Ed. 1140, 35 Sup. Ct. Rep. 717.

²¹ See note in 16 L. R. A. (N. S.) 1165.

if insurance contracts are so different from all other contracts that in them the danger of fraud and injustice is greater if the contract is strictly enforced than if parol evidence is admitted to vary its terms.

We have seen that by the weight of authority an agent, except a mere solicitor, has implied authority orally to change or waive the provisions of an insurance contract in the face of a clause in the policy to the contrary; that in reaching this result the courts have gone contrary to the common law of agency and have ridden rough-shod over the parol evidence rule where necessary; that the decisions of the majority can be justified only on the ground of public policy; that in conditional sale and construction contracts where exactly similar considerations of public policy arise, the courts refuse to depart from the common law of agency.

It may be that the majority are right and that public policy requires that whenever a principal deals through an agent he be not allowed to limit the ostensible authority of his agent by provisions in any contract. But such a change in our law of agency is so fundamental that it should not be made by the courts, but by the legislature. Further, I do not believe that in insurance contracts justice between the parties requires such a change in our law. I think that the ignorance of the portion of our population who take out insurance is greatly over-estimated by the courts. This is especially true in fire insurance, which is never taken out by the submerged tenth, but by property-owners: the same class in our population who execute deeds, mortgages and contracts. Every one of the twenty-seven states²² which have prescribed the form of fire insurance contracts have required that the contract contain a clause limiting the authority of agents to vary the contract orally. The true remedy for the situation is the one that these states are now using, to have the legislature or a state insurance commissioner prescribe just what conditions an insurance policy shall contain, so that neither party will have an undue advantage over the other.

San Francisco, California.

Sam B. Warner.

²² Arizona, California, Connecticut, Georgia, Idaho, Iowa, Louisiana, Maine, Massachusetts, Michigan, Minnesota, Nebraska, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Texas, Utah, Washington, West Virginia and Wisconsin.